

Employment Update

Taxation of senior management staff pay-outs

29th November 2019

In connection with the judgement of the Supreme Court (Administrative litigation Chamber) of 5 November 2019

1.- Between labour court and administrative litigation, one of the most controversial and controversial issues was the different consideration of whether the compensation for withdrawal or dismissal of senior management staff established in Royal Decree 1382/1985 of 1 August 1985, which regulates the special employment relationship of senior management staff, constituted a minimum necessary right and, as a logical consequence, whether the 7 or 20 days per year of service, respectively, provided for in the law, should be exempt from taxation.

The labour courts, both Superior Courts of Justice of the respective Autonomous Communities and the Supreme Court itself, indicated that the compensation provided for executive personnel was minimal, that it could be improved, but not reduced or suppressed. However, and despite this, the jurisprudential line of the Third Chamber (Cont. Adm.) of the Supreme Court, declared that the compensation in the case of senior management relationship was subject in its entirety, with the argument that the Royal Decree did not establish any limit, either minimum or maximum, of a mandatory nature, with respect to the compensation of senior management personnel, given that those indicated in article 11 were "in the absence of a pact" and "in the absence thereof" and therefore merely subsidiary to what had been agreed.

2.- The controversy has fortunately come to an end. In fact, on November 5, 2019, the Second Section of the Third Chamber (Cont.-Adm.; RC 2727/2017) has issued a judgment establishing as an interpretative criterion that:

"It must be understood that in the event of termination of the senior management contract due to waiver by the employer there is a right to a mandatory minimum compensation of 7 days' salary per year of work, with a limit of six monthly payments and, therefore, that the amount of compensation is exempt from taxation in Personal Income Tax, under Article 7.e) of the revised text of the Personal Income Tax Law, approved by Royal Legislative Decree 3/2004, of 5 March.

The change of criteria is justified by the Supreme Court in its reference to the doctrine issued by the Social Chamber in its judgement of 22 April 2014. This allows overcoming the previous judicial interpretation on the submission of compensation to IRPF because since that ruling has confirmed the mandatory nature of compensation, and as the State Attorney pointed out in the appeal, it is the Social Chamber that has the final word in the interpretation of Article 11 of RD 1382/1985, as it is a rule specific to the social branch of law and a matter whose full knowledge corresponds to that jurisdiction.

3.- We must draw attention to the background of the case and the excessive passage of time from the contractual termination to the recent final resolution of the litigation (13 years).

The high court ruling confirmed the decision of 8 March 2017, handed down by Section 4 of the Administrative Litigation Chamber of the National High Court, which upheld administrative appeal No. 242/2015, against the decision of the Central Economic-Administrative Court of 5 February 2015 (claim 3696/2011), dismissal of the complaint against the agreements of the Deputy Head of the Technical Office of the Tax and Customs Control Unit, Central Delegation of Large Taxpayers, of 27



May 2011 and 5 October 2011, for which final settlement was made, respectively, for the concept of personal income tax withholding, fiscal year 2006, and sanctioning resolution for the same concept and period.

The ruling of the High Court annulled the Central Economic Administrative Tribunal's (TEAC) resolution, as well as the liquidation and sanction originally challenged, considering that it was not obliged to withhold the indemnity paid due to their termination as senior management personnel, as this income is exempt from Personal Income Tax, as it is mandatory up to a limit of 7 days' salary per year of work and up to a maximum of 6 months' salary.

Moreover, the entire judicial process was caused by a senior management contract that ended on 18 July 2006 with the payment of compensation to the employee of € 37,770.01, on which no withholding was made on account of personal income tax as it was considered exempt under Article 7.e) LIRPF (personal income tax law).

4.- An important consideration. Although the Supreme Court ruling only mentions the exemption from compensation for withdrawal, similar reasoning could be considered and therefore transferred to those set forth in the same *mutatis mutandis*, and, therefore, the same criterion to the amount of 20 days per year of service with the limit of 12 monthly payments established in the Royal Decree of Senior Management for cases of unfair dismissal.

5.- And a final reflection. This ruling may oblige the Tax Agency (AEAT) to correct its criteria and allow executives whose contract has been terminated, whether by withdrawal or dismissal, in the last four years to claim what the AEAT has improperly claimed. In general, the reimbursement of undue income from indemnities received by senior managers in 2015, 2016, 2017 and 2018 could be requested.

You can read the [full sentence](#) for more information.

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